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This edition of Newsflash is all about claiming depreciation, whether you are a property investor or in business. Please don't hesitate to share Newsflash with your friends. They can even sign up to have each edition emailed to them, by going to the bottom right of this page http://www.bantacs.com.au/media-library/newsflash/

Scrapping Plant and Equipment on a Rental Property Nowadays

How does scrapping affect the original purchase price of the property, for CGT purposes, now that depreciation can't be claimed on second hand plant and equipment (P&E)?

If you buy an established property the P&E in it are considered second hand to you. It is the same if you first live in a property, even a brand new one, before you rent it out. Property investors are no longer allowed a tax deduction for depreciation on second hand P&E.

So, what happens when you have to replace that P&E and scrap the old piece? Well as long as the replacement P&E is brand new you can start claiming its depreciation against your rental income.

When you throw out or scrap the old piece of P&E its value, when you purchased the property, is removed from the original purchase price of your house for the house's CGT cost base. You also get a capital loss for that value of the P&E which you can offset against capital gains you have that year or in the future.

The scrapping of the old P&E is CGT event K7 section 104-235 ITAA 1997. CGT event K7 is not new, it is just being widened to make sure that it is clear it includes P&E that is not tax deductible under the new laws. CGT event K7 has always applied to non tax deductible P&E in a house. We have always just chosen to ignore it because it all comes out in the wash. Capital losses are quarantined and can only be used to offset a capital gain, not other income.

Here is how you would calculate a capital gain strictly according to K7 when you scrap a piece of equipment worth $200, for which you could not claim a tax deduction, in a house you bought for $500,000. Then the next year you sell the property with no other CGT events in between.

Scrapping Year:
In your CGT records reduce the cost base of the property to $499,800
In your tax return carry forward a capital loss of $200.

Sale Year:
Sell property for $600,000 with cost base of $499,800 so $100,200 capital gain but as have a carried forward capital loss of $200 from the scrapping year then capital gain is reduced to $100,000.

How it works in the real world:
Ignore anything to do with the scrapping of the P&E so when you sell the property for $600,000 the cost base is still $500,000 and there is no carried forward capital loss. This gives you a capital gain of $100,000.

In past CGT event K7 has been ignored, even by the ATO because it all comes out in the wash. I doubt whether this will change as the only time it will make any difference is if, between the scrapping and the sale of the property, the taxpayer makes a capital gain that they could offset the carried forward capital loss from the scrapping against and then the difference is only one of timing not amount. You can see why the ATO is not concerned about going into the detail of CGT event K7, it is only an advantage to the taxpayer. From the taxpayer's point of view it would probably be more trouble and accounting fees than it was worth but a lot depends on the amount of P&E scrapped.

Quantity surveyors are all over this saying they can prepare you a report when you buy a property breaking down the value of all the P&E so you can comply with the new laws. A quantity surveyor's report is not necessary, you are allowed to estimate the value of the P&E yourself.

What isNew from the ATO – Small Business $20,000 Plant & Equipment Write Off

Unless it is extended in the May budget the small business concession of being able to immediately write off any plant and equipment costing less than $20,000 will finish at 30th June, 2018. Just 4 months from now.

The very, very urgent point here is to start planning your expenditure now. Even if it is feasible to hold off to see what the May budget offers, you need to be thinking about your likely capital expenditure over the next few years and the relevant taxable income. Make sure you speak to your Accountant, you don't want to spend so much money that it brings your taxable income down to a low or zero tax rate.

It is all well and good if you spend the money in a high-income year. But what happens when you do your year end accounts and realise that it wasn't that good a year after all? All is not completely lost; the small business concessions are optional. You can opt out and just claim the depreciation slowly over the expected life of the plant and equipment but if you didn't really need to spend the money that soon your cashflow is going to suffer unnecessarily without the corresponding tax boast to pick it up. You see if you do opt out of the small business concessions it will be for all the plant and equipment you buy that year, you can't pick and choose.

This Week's Webinar

The whole scrapping issue in general is not as simple as the quantity surveyors make out. For example when claiming building depreciation you have to take into account the use of the property by previous owners https://www.youtube.com/watch?time_continue=198&v=Yq9Z3wnXPpY

Best Askbantacs Question – Refinancing a Loan through Parents

Making sure the interest paid to parents continues to be tax deductible http://taxquestions.com.au/parentloan/

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